LIBRARY
SUPREME COURT, U. S.

Supreme Court, U. S.
FILED
AUG 29 1973
MICHAEL RODAK, JR., CLERK

In the

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1973

No. ~~73~~ - 374

UNION EQUITY COOPERATIVE EXCHANGE INC.,
Petitioner,

VERSUS

COMMISSIONER OF THE INTERNAL REVENUE,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

FRANK CARTER
Bass Building
Enid, Oklahoma

Counsel for Petitioner

of Counsel:

CARTER & CARTER
Bass Building
Enid, Oklahoma

August, 1973

UTTERBACK TYPESETTING CO., 519 W. CALIF., OKLAHOMA CITY, PH. 235-0030

TABLE OF CONTENTS

	PAGE
Opinions Below	1
Jurisdiction	2
Statutes and Regulations Involved	2
Questions Presented	4
Statement of the Case	5
Argument	7
The patronage dividends paid by Petitioner to its member patrons, representing their proportionate share of the earnings developed by business transacted by them with the Petitioner during the year ending March 31, 1963, belonged exclusively to them, and cannot be eroded or diluted	7
Conclusion	14

Certificate of Service follows Brief—

Appendix is in separate volume

TABLE OF AUTHORITIES

CASES:

CIR v. Hansen, 1959, 79 S.Ct. 1270, 360 U.S. 446, 3 L.Ed.2d 1360	13
Des Moines County Farm Service Company v. U. S., 324 F.Supp. 1216 (S.D. Iowa 1971), affirmed 448 F.2d 776, by the Eighth Circuit	11

AUTHORITIES CONTINUED PAGE

Farmers Cooperative v. Birmingham, 86 F.Supp. 201 8

Federal Power Commission v. Tuscarora Indian Nation, App. D.C. 1960, 80 S.Ct. 543, 362 U.S. 99, 4 L.Ed.2d 584, rehearing denied 80 S.Ct. 858, 362 U.S. 956, 4 L.Ed.2d 873 12

F.T.C. v. Flotill Products, Inc., Cal. 1967, 88 S.Ct. 401, 389 U.S. 179, 19 L.Ed.2d 398 13

Heflin v. U. S., Ala. 1959, 79 S.Ct. 451, 358 U.S. 415, 3 L.Ed.2d 407 13

Jarecki v G. D. Searle & Co., Ill. 1961, 81 S.Ct. 1579, 367 U.S. 303, 6 L.Ed.2d 859 12

Knetsch v. U. S., Cal. 1960, 81 S.Ct. 1579, 367 U.S. 303, 6 L.Ed.2d 859 12

Mitchell v. Robert De Mario Jewelry, Inc., Ga. 1960, 80 S.Ct. 332, 361 U.S. 288, 4 L.Ed.2d 323 13

N.L.R.B. v. Metropolitan Life Ins. Co., R.I. 1965, 85 S.Ct. 1061, 380 U.S. 438, 13 L.Ed.2d 951 12

Monroza v. Carbon Black Export, Inc., Tex. 1959, 79 S.Ct. 710, 359 U.S. 180, 3 L.Ed.2d 723, rehearing denied 79 S.Ct. 1115, 359 U.S. 999, 3 L.Ed.2d 986 13

Rogers v. Quan, App. D.C. 1958, 78 S.Ct. 1076, 357 U.S. 193, 2 L.Ed.2d 1252 13

Saenger v. Commissioner, 69 F.2d 613 8

San Joaquin Valley Poultry Producers Association v. Commissioner, 136 F.2d 382 8

State of Mississippi v. Morgan Gin Company, 189 So. 187 ..... 8, 9

U. S. v. Mississippi Chemical Company (U. S. Court of Appeals, Fifth Circuit No. 19418, decided January 9, 1964, 326 F.2d 569) 7, 8, 10, 12

U. S. v. Price, Ariz. 1960, 80 S.Ct. 326, 361 U.S. 304, 4 L.Ed.2d 334 13

AUTHORITIES CONTINUED

PAGE

Waterman S. S. Corp. v. U. S., Ala. 1965, 85 S.Ct. 1389, 381 U.S. 252, 14 L.Ed.2d 370, rehearing denied 86 S.Ct. 17, 382 U.S. 873, 15 L.Ed.2d 114 ___ 12

STATUTES:

2 O.S.A., § 361 L ___ 3-4
2 O.S.A., § 361 w ___ 3

18 O.S.A., § 1.132 ___ 2
18 O.S.A., § 1.70 ___ 2-3

26 U.S.C., § 172 ___ 4
26 U.S.C.A., § 461 ___ 4

28 U.S.C.A., § 1254 (1) ___ 2

MISCELLANEOUS:

7 AFTR2d 650 ___ 8

Colony Farms 688 ___ 8

In the
Supreme Court of the United States

OCTOBER TERM, 1973

No. ————

UNION EQUITY COOPERATIVE EXCHANGE INC.,
Petitioner,

VERSUS

COMMISSIONER OF THE INTERNAL REVENUE,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

Union Equity Cooperative Exchange Inc., your Petitioner, prays that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the Tenth Circuit, entered in the above entitled case on July 2, 1973, with mandate stayed until August 26, 1973.

OPINIONS BELOW

The court rendered its opinion adversely to its Petitioner, on July 2, 1973, a copy of which is hereto attached and marked Appendix "A."

Thereafter, on July 17, 1973, your Petitioner filed its application for a stay of the mandate, pending an appli-

cation to the United States Supreme Court for a Writ of Certiorari, a copy of which is (Appendix "B").

On July 27, 1973, the Circuit Court stayed the Order and Decree and stayed the mandate until August 26, 1973, pending the timely filing by your Petitioner for a Petition for a Writ of Certiorari in the Supreme Court of the United States, a copy of which is (Appendix "C").

JURISDICTION

The judgment of the Court of Appeals was entered on July 2, 1973. A Motion to Modify the Decree, and an Order staying the mandate until August 26, 1973 was entered on July 27, 1973. The jurisdiction is invoked under the provisions of Title 28, U.S.C.A. 1254 (1).

STATUTES AND REGULATIONS INVOLVED

Oklahoma Statutes Annotated, Title 18, *Corporations*

Title 18, § 1.132, Dividends payable in cash or property:

> "a. Subject to any further limitations or restrictions in the articles of incorporation, a domestic corporation may, by resolution of its board of directors, declare and pay dividends in cash or property only as follows:
>
> "(1) Out of earned surplus; . . ."

Oklahoma Statutes Annotated, Title 18, *Corporations*

Title 18, § 1.70, Books of account:

> "Except as otherwise provided in Section 16 of this Act, every corporation shall keep and maintain adequate and correct accounts of its properties and busi-

ness transactions, including accounts of its assets, liabilities, receipts, disbursements, gains, losses, capital, surplus, and shares. The books of account shall at all reasonable times be open to inspection by any director. Laws 1947, p. 110, § 70."

Oklahoma Statutes Annotated, Title 2, *Agriculture*

Title 2, § 361 w, Application of general business corporation laws:

"The provisions of the general business corporation laws of this State and all powers and rights thereunder shall apply to the associations organized hereunder, except where such provisions are inconsistent with the express provisions of this Act. Laws 1937, p. 268, §24."

Oklahoma Statutes Annotated, Title 2, *Agriculture*

Title 2, § 361 L, Dividends and Earnings:

"(b) Dividends and Earnings. The directors, subject to the revision by the members or stockholders, at any general or special meeting lawfully called shall apportion the net earnings thereof from time to time at least once in each year. Such apportionment shall not be made until not less than ten (10) per cent of any undistributed balance accruing since the last apportionment, has been set aside in a surplus or reserve fund unless such surplus or reserve funds equal at least one hundred (100) per cent of the paid up membership fees or capital stock.

"(c) An association shall limit the interest it pays on membership capital or stock to an amount not greater than eight (8) per cent per annum.

"(d) Undistributed balances from any source, in excess of additions to reserves and surplus, shall be

distributed on the basis of patronage, that is according to the amount or value, as the association may decide, of the products sold to or through, and/or purchased from or through, the association by its patrons. . . ."

U.S.C. Annotated, Title 26, Internal Revenue Code

Title 26, § 461, General rule for taxable year of deduction:

"(a) General rule.—The amount of any deduction or credit allowed by this subtitle shall be taken for the taxable year which is the proper taxable year under the method of accounting used in computing taxable income."

U.S.C., Title 26, § 172

[¶14,561] Code § 172. Net Operating Loss Deduction:

"(a) Deduction Allowed.—There shall be allowed as a deduction for the taxable year an amount equal to the aggregate of (1) the net operating loss carryovers to such year, plus (2) the net operating loss carrybacks to such year. For purposes of this subtitle, the term 'net operating loss deduction' means the deduction allowed by this subsection. . . ."

QUESTIONS PRESENTED

(1) Whether or not the patrons of a duly organized Farm Cooperative, in Oklahoma, can be deprived of the right to receive their *patronage dividends* (representing their own money, and to pay taxes thereon themselves), without being subjected to the levy of a separate and additional Corporate tax being assessed thereon by the Commissioner, and per force, paid, and deducted by their Marketing Cooperative?

(2) Whether or not the patrons of a Farm Cooperative through their by-laws, and directors, have the right to require their cooperative to pay stock dividends from *surplus reserves* without reducing their patronage dividends?

(3) Which of the conflicting decisions of the Fifth Circuit Court of Appeals (326 F.2d (569), and the Eighth Circuit (448) F.2d (776) involving the same issues as presented in this case, should prevail?

A Certificate of Service has been prepared, and is hereto attached.

STATEMENT OF THE CASE

Union Equity Cooperative Exchange Inc., your Petitioner, hereinafter referred to as "UNION EQUITY" is an Oklahoma Cooperative Marketing Association doing business pursuant to the Oklahoma Marketing Act, and the Capper-Volstead Act (R. 41).

It has been so engaged, since its date of incorporation in October of 1929 (R. 41).

Its principal office is and was on January 22, 1970, in Enid, Oklahoma.

As of the close of business on March 31, 1963, Union Equity was doing business as a *non-exempt* cooperative. Since that date, pursuant to a letter of exemption granted under IRC 521, Union Equity has carried on business as an *exempt* farmers cooperative.

During the critical periods involved in this proceeding, its fiscal and tax year, extended from April 1, to March 31 of each year.

That it filed its annual tax returns for the years 1961, 1963, and 1964, and which were duly filed by its competent and outside accountants.

For the taxable year, ending March 31, 1963, your Petitioner from the earnings, paid tax on $476,410.65, which it transferred to its surplus reserve, and for the year ending March 31, 1964, it allocated $245,112.50 pursuant to its by-laws and actions of its Board of Directors to its general reserve, and thereupon declared a 2½ per cent dividend on the outstanding stock. (Union Equity paid tax on the $245,112.50 for its tax year ending March 31, 1964, even though it was then "exempt.")

Thereafter, and on October 30, 1969, the Commissioner of Internal Revenue issued a notice of deficiency, claiming in substance:

1. That for the year ending March 31, 1963, there was a deficiency of $138,164.30 in taxes, and for the taxable year ending March 31, 1961, in the amount of $81,267.77.

These were asserted taxes on amounts paid out by the Company, to its patrons, representing their earnings for patronage. The Commissioner contended that these were amounts which represented taxes due on improperly distributed "patronage earnings." (Even though these amounts definitely represented sums due the patrons (under Charter and By-Law) by virtue of their business with the Petitioner during those years.)

On appeal to the Tax Court, the Tax Court finally adjudicated in favor of the Commissioner.

A Petition for Review was filed with the Tenth Circuit Court of Appeals.

The Tenth Circuit Court of Appeals then, after several weeks, and upon the dates hereinabove indicated, rendered its opinion and order adversely to your Petitioner (Appendix "A").

ARGUMENT

THE PATRONAGE DIVIDENDS PAID BY PETITIONER TO ITS MEMBER PATRONS, REPRESENTING THEIR PROPORTIONATE SHARE OF THE EARNINGS DEVELOPED BY BUSINESS TRANSACTED BY THEM WITH THE PETITIONER DURING THE YEAR ENDING MARCH 31, 1963, BELONGED EXCLUSIVELY TO THEM, AND CANNOT BE ERODED OR DILUTED.

In support of this assertion, Petitioner alleges that it is fully fortified by the holding and decision in the case of *U. S.* v. *Mississippi Chemical Company* (U. S. Court of Appeals, Fifth Circuit No. 19418, decided January 9, 1964, 326 F.2d 569).

This case was first tried to a Federal jury in Vicksburg, Mississippi, with proper instructions given by the court; and pursuant to the verdict of the jury, the court rendered a judgment in favor of the taxpayer, which involved a very similar and analogous situation as now presented by Union Equity Cooperative Exchange.

Mississippi Chemical was a Consumer Cooperative. The factual situation only differs from the instant case before the Court in that Mississippi Chemical was a farmers cooperative, engaged in the supply of fertilizer to its mem-

bers, as a non-exempt cooperative, and to others; while Union Equity is a *marketing* farmers' cooperative engaged in the storage and marketing of wheat and grain for its members, and non-members.

In the *Mississippi Chemical* case, herein referred to, pursuant to its pre-existing obligations contained in its charter and by-laws, it paid out some $680,000.00 during a period of four years, representing patronage refunds.

The government objected for the reason that such payments were in excess of the amounts which would have been payable under the formula set forth in its AFF 6967. The company contended, as the Petitioner does in this case, that such payments did not constitute income to the taxpayer but belonged to the stockholder patrons under their legally enforceable contract; and that said sum never became the property of the corporation.

The District Court held in favor of the taxpayer, after a trial by jury, and proper instructions by the court, which is cited in 7 AFTR2d 650; and in support thereof, cited the cases of *San Joaquin Valley Poultry Producers Association* v. *Commissioner*, 136 F.2d 382; *Farmers Cooperative* v. *Birmingham*, 86 F.Supp. 201; *Colony Farms* 688; *Saenger* v. *Commissioner*, 69 F.2d 613; and *State of Mississippi* v. *Morgan Gin Company*, 189 So. 187.

That case was decided February 7, 1961.

It was appealed by the Commissioner, to the United States Court of Appeals, for the Fifth Circuit, and was affirmed by that Court on January 9, 1964, and is reported in 326 F.2d 569.

In that case, it was urged on appeal by the government that in the distributions made by Mississippi Chemical, it had not complied with the applicable regulations promulgated by the department.

In affirming the decision of the lower court, the Fifth Circuit among many other pertinent determinations held:

> "The Treasury Department cannot, by interpretative regulations, make income of that which is not income within the meaning of the Revenue Acts of Congress. Treasury regulations can add nothing to income as defined by Congress."

On checking the procedures applicable to a review of this case of the Fifth Circuit, we find that no writ of certiorari was ever granted.[1]

The case of Union Equity, as currently submitted to this Honorable Court, is to all intents and purposes perfectly analogous and is entitled to serious consideration.

In this connection Petitioner emphasizes the contents and relevancy of ¶20 of the Stipulation. (See App.)

In this paragraph it is tacitly stipulated that for thirteen years, since 1950 (as a matter of fact, for nineteen years—until 1969), the method of accounting adopted and utilized by Petitioner in computing its patronage dividend deductions, had always charged its capital stock dividend to non-member business or to the surplus reserve. And that during those years the Internal Revenue Service had made periodic audits of Petitioner's tax return and the

---

[1] Incidentally this case was tried and won by Mr. Satterfield of Mississippi, past President of the American Bar Association—representing the Taxpayer.

question of proper allocation of stock dividends had never been previously questioned by the examining agent.

This practice, of course, on the part of the Respondent raises immediately the question of: "Equitable Estoppel." In other words, as the result of this consistent method of paying dividends on capital stock out of non-member business, or out of the surplus reserve, by this Petitioner, Respondent has fortified the encouragement of this Petitioner to follow the "Law of Cooperation" and to insulate all possible net earnings of member-patrons against the encroachment into their earnings.

All recipients of such dividends of patronage are required to report them as taxable income and to pay tax thereon at their respective rates.

After nineteen years of conformity with this method of accounting being followed by Petitioner, and with full reliance upon the tacit agreement of the Respondent that Union Equity was in compliance with the law, it would be obviously inequitable to abruptly force this Petitioner to accept and adhere to an adverse ruling on this assessment for the years 1963 and 1964.

THE CONFLICT IN DECISIONS BY THE FIFTH, EIGHTH, AND THE TENTH CIRCUIT, ESPECIALLY DESERVES ATTENTION FROM THIS COURT, IN ORDER TO RESOLVE SUCH CONFLICTS.

Reference has been made *supra* to the case of *U. S.* v. *Mississippi Chemical Company,* Fifth Circuit, 326 F.2d 569.

In all fairness, it should be pointed out in this Petition that there does not exist a contrary decision from the Eighth Circuit Court of Appeals.

We refer to the case of *Des Moines County Farm Service Company* v. *U. S.*, 324 F.Supp. 1216 (S.D. Iowa 1971), *affirmed* 448 F.2d 776, by the Eighth Circuit.

The *Des Moines* case, above referred to, had a very similar tax situation as encountered by the Fifth Circuit, in the *Mississippi* case, and also by the current case of Union Equity, in the Tenth Circuit. In the *Des Moines* case, *supra*, the Court sustained the Internal Revenue Service, but did so in the opinion of your Petitioner, entirely without recognition of the rights of the individual producer, who was a patron of the organization, and who under the many rules and regulations set forth for the protection of member patrons was entitled to payment without adulteration or reduction.

Under the theory of a farmers' cooperative association, the farmer producer is entitled to all of his share of the proceeds derived from the marketing of his product. There is no provision whatever in either of the State or Federal acts which authorize the dilution of his patronage dividends.

In the Iowa case, *supra*, the Court arbitrarily reduced his interest in the cooperative (proceeds from the sale of his product).

The earnings derived from the sale or marketing of the product of a member belongs to him. The cooperative is merely an agent, or "conduit," for the transmission of the value of his product to him after deducting the cost of processing and sale. It makes no difference if the cost of such sale may be reduced by other income. He is entitled to the net. Presumably the sales organization, the coopera-

tive, will utilize all legitimate means to reduce this cost, but its sole purpose is to accentuate and develop and improve the net amounts payable to the member producer, from his product.

The *Mississippi* case, *supra*, upheld this theory.

Your Petitioner feels that it is organized, and operating solely for the benefit of its member producers. If it develops any additional income from non-members, that amount, under the laws of Oklahoma as indicated herein, may be transferred to surplus and dividends paid on stock therefrom without invasions of the amounts and proceeds due to the producers from their respective deliveries and sales through the cooperative.

For authorities justifying assumption of jurisdiction of the United States Supreme Court, relating to cases involving previous conflicts of decisions concerning the same or similar questions, see the following:

—*Waterman S. S. Corp.* v. *U. S.*, Ala. 1965, 85 S.Ct. 1389, 381 U.S. 252, 14 L.Ed.2d 370, *rehearing denied* 86 S.Ct. 17, 382 U.S. 873, 15 L.Ed.2d 114;

N.L.R.B. v. *Metropolitan Life Ins. Co.*, R.I. 1965, 85 S.Ct. 1061, 380 U.S. 438, 13 L.Ed.2d 951;

Jarecki v. *G. D. Searle & Co.*, Ill. 1961, 81 S.Ct. 1579, 367 U.S. 303, 6 L.Ed.2d 859;

Knetsch v. *U. S.*, Cal. 1960, 81 S.Ct. 1579, 367 U.S. 303, 6 L.Ed.2d 859;

Federal Power Commission v. *Tuscarora Indian Nation*, App. D.C. 1960, 80 S.Ct. 543, 362 U.S. 99, 4 L.Ed.2d 584, *rehearing denied* 80 S.Ct. 858, 362 U.S. 956, 4 L.Ed.2d 873;

Mitchell v. *Robert De Mario Jewelry, Inc.*, Ga., 1960, 80 S.Ct. 332, 361 U.S. 288, 4 L.Ed.2d 323;

U. S. v. *Price*, Ariz. 1960, 80 S.Ct. 326, 361 U.S. 304, 4 L.Ed.2d 334;

Monroza v. *Carbon Black Export, Inc.*, Tex. 1959, 79 S.Ct. 710, 359 U.S. 180, 3 L.Ed.2d 723, *rehearing denied* 79 S.Ct. 1115, 359 U.S. 999, 3 L.Ed.2d 986;

Heflin v. *U. S.*, Ala. 1959, 79 S.Ct. 451, 358 U.S. 415, 3 L.Ed.2d 407;

Rogers v. *Quan*, App. D.C. 1958, 78 S.Ct. 1076, 357 U.S. 193, 2 L.Ed.2d 1252;

CIR v. *Hansen*, 1959, 79 S.Ct. 1270, 360 U.S. 446, 3 L.Ed.2d 1360;

F.T.C. v. *Flotill Products, Inc.*, Cal. 1967, 88 S.Ct. 401, 389 U.S. 179, 19 L.Ed.2d 398.

CONCLUSION

Your Petitioner therefore respectfully represents to the Court that there apparently does exist a difference in the theory of cooperatives, between and among the Fifth, Eighth, and Tenth Circuit; and that it should be resolved by this Court at the earliest possible date.

HENCE this Petition of a Writ of Certiorari.

Respectfully submitted,

FRANK CARTER
Bass Building
Enid, Oklahoma

Counsel for Petitioner

of Counsel:

CARTER & CARTER
Bass Building
Enid, Oklahoma

August, 1973

CERTIFICATE OF SERVICE

Three true and correct copies of this petition for writ of certiorari have this day been mailed, postage prepaid, to:

Honorable Scott Crampton
Asst. Attorney General
Tax Division, Department of Justice
Washington, D. C. 20530

Department of Justice, Washington
Tax Division
Attn: Mrs. Carolyn Just
Washington, D. C. 20530

Mr. Howard K. Phillips, Clerk
United States District Court
Tenth Circuit
Denver, Colorado Mailed one copy

FRANK CARTER